

Internal Revenue Service
memorandum

TL-N-7295-89

CC:TL:TS

CTSANDERSON

date: SEP 8 1989

to: District Counsel, Jacksonville SE:JAX
Attn: Stephen R. Takeuchi

from: Assistant Chief Counsel (Tax Litigation) CC:TL

subject: I.R.C. §§ 6621(c) and 6230(a)(2)

This memorandum is in response to your memorandum requesting tax litigation advice, dated May 26, 1989.

ISSUE

Whether legislation should be proposed to amend I.R.C. § 6621(c)(4) to expressly confer jurisdiction on the Tax Court to determine the applicability of section 6621(c) interest when it is the subject of an affected items statutory notice of deficiency issued under I.R.C. § 6230(a)(2)(A)(i).

CONCLUSION

We are aware of the problems that exist concerning the Tax Court's jurisdiction over section 6621(c) interest raised in an affected items statutory notice of deficiency ("SND"). Because of these problems, we will give due consideration to recommending appropriate legislation or regulations the next time we put together a legislative or regulatory proposal concerning the TEFRA partnership provisions.

DISCUSSION

I.R.C. § 6621(c)(1) provides for an additional rate of interest payable under I.R.C. § 6601 with respect to "substantial underpayment[s] attributable to tax motivated transactions." The issue of whether a transaction is tax motivated, as defined in I.R.C. § 6621(c)(3), is decided at the partnership level. However, for an underpayment to be "substantial" for these purposes, the amount of the underpayment attributable to the tax motivated transaction must exceed \$1,000. I.R.C. § 6621(c)(2). This determination must be made at the partner level.

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The additional rate of interest under I.R.C. § 6621(c) constitutes an "affected item" under I.R.C. § 6231(a)(5). N.C.F. Energy Partners v. Commissioner, 89 T.C. 741 (1987). Its application to the particular partner "turns on the amount of the taxpayer's underpayment attributable to a tax motivated transaction," a determination that has to be made at the partner level. Id. Therefore, this item is more than a "computational adjustment" under I.R.C. § 6231(a)(6).
Id. 1/

I.R.C. § 6230(a) provides in relevant part:

(a) **Coordination With Deficiency Proceedings.--**

(1) **In general.--**Except as provided in paragraph (2), subchapter B of this chapter shall not apply to the assessment or collection of any computational adjustment.

(2) **Deficiency proceedings to apply in certain cases.--**

(A) Subchapter B shall apply to any deficiency attributable to--

(i) affected items which require partner level determinations, or

(ii) items which have become nonpartnership items (other than by reason of section 6231(b)(1)(C)) and are described in section 6231(e)(1)(B).

Pursuant to this section, "[o]nce the partnership level proceeding is completed, respondent in some circumstances may issue a notice of deficiency to the partner determining additional deficiencies attributable to affected items." N.C.F. Energy Partners, 89 T.C. at 743-744 (emphasis added).

A. Section 6621(c) as Sole Subject of SND

I.R.C. § 6230(a), while authorizing the issuance of individual SNDs pursuant to subchapter B, did not change what

1/ The conclusion that the additional rate of interest under I.R.C. § 6621(c) is more than a mere "computational adjustment" is somewhat contradicted by Temp. Treas. Reg. § 301.6231(a)(6)-1(b), which provides that a "computational adjustment includes any interest due with respect to any underpayment. . . ." Section 6621(c) simply provides for an increased rate of interest; it is not an addition to tax or additional amount under subchapter A of chapter 68. In any event, as discussed below, the result would be the same if I.R.C. § 6621(c) interest was a "computational adjustment."

constitutes a deficiency that can be the subject of such a SND. Interest, including I.R.C. § 6621(c) interest, is not included in the definition of deficiency and cannot be the sole subject of a SND. See I.R.C. §§ 6211(a), 6212(a), 6601(e)(1) and 6621(c)(4). The deficiency procedures under subchapter B of chapter 63 do not apply to interest. I.R.C. § 6601(e)(1).

Additionally, the Tax Court would not have jurisdiction to make a redetermination concerning a SND solely covering interest. Generally, the court lacks jurisdiction to decide issues concerning interest. Transport Manufacturing & Equipment Co. v. Commissioner, 434 F.2d 373, 381 (8th Cir. 1970); Commissioner v. Kilpatrick's Estate, 140 F.2d 887 (6th Cir. 1944); Engh v. United States, 658 F. Supp. 698 (N.D. Ill. 1987); cf. Baumgardner v. Commissioner, 85 T.C. 445 (1985) (concluded that the court had jurisdiction to consider payments of interest as part of an overpayment under I.R.C. § 6512(b)'s grant of jurisdiction to determine overpayments).

In 1984, Congress extended the court's jurisdiction to allow it to determine the portion of the deficiency which is a substantial underpayment attributable to tax motivated transactions:

(4) Jurisdiction of Tax Court.-- In the case of any proceeding in the Tax Court for a redetermination of deficiency, the Tax Court shall also have jurisdiction to determine the portion (if any) of such deficiency which is a substantial underpayment attributable to tax motivated transactions.

I.R.C. § 6621(c)(4).

However, Congress did not amend the definition of a deficiency under section 6211 to include a determination under section 6621(c). Therefore, the Tax Court's extended jurisdiction is contingent upon there being a deficiency before the court. See I.R.C. § 6621(c)(4). Accordingly, just as the court would lack jurisdiction over a section 6621(c) issue prior to the conclusion of a TEFRA partnership level proceeding as held in N.C.F. Energy Partners, 89 T.C. 741, the court would also lack jurisdiction over such an issue after the proceeding if it was the sole item raised in an affected item SND.

B. SND Raising Section 6621(c) Add-on Interest and Other Affected Items which Constitute a Deficiency

Even if there are other affected items raised in the SND which constitute a deficiency, a literal reading of section 6621(c)(4) could lead to the conclusion that the Tax Court would still lack jurisdiction over section 6621(c) interest attributable to partnership items. The statute provides that

"[i]n the case of any proceeding in the Tax Court for a redetermination of deficiency, the Tax Court shall also have jurisdiction to determine the portion (if any) of such deficiency which is a substantial underpayment attributable to tax motivated transactions." I.R.C. § 6621(c)(4) (emphasis added). If the "substantial underpayment" is attributable to a partnership item, arguably the Tax Court would not have jurisdiction to determine the applicability of section 6621(c) since that deficiency (i.e., the partnership item deficiency) is not before the court in an action on an affected items SND.

For example, if the negligence penalty and section 6621(c) interest are affected items remaining after the settlement of a partnership item, the negligence penalty is a deficiency that can be the subject of an affected items SND. See I.R.C. § 6662(b). This deficiency, however, cannot constitute a "substantial underpayment attributable to a tax motivated transaction." Temp. Treas. Reg. § 301.6621-2T, A-12. Thus, arguably there is no deficiency before the court within the purview of section 6621(c)(4).

Under similar facts in a non-TEFRA context (i.e., negligence and section 6621(c) are the only items at issue) our position is that section 6621(c) should not be raised in the SND and could be immediately assessed; the taxpayer could then challenge the assessment of the interest in a refund posture. These same rules should apply with an affected items SND since affected items are subject to the same rules concerning deficiency procedures. See I.R.C. § 6230(a)(2)(A)(i). Therefore, in the future an affected items SND under the above scenario should never include section 6621(c).

We had previously concluded in an informal tax litigation advice to include section 6621(c) in an affected items SND under the above described scenario. This conclusion was reached by focusing on the TEFRA refund provisions as opposed to the deficiency procedures. The TEFRA refund provisions would not be available to the taxpayer under this scenario. See I.R.C. §§ 6227, 6228, 6230(c) & (d). Therefore, we concluded that a prudent approach would be to include section 6621(c) in an affected items SND since a court could hold that otherwise the taxpayer would not have a forum to challenge the tax motivation determination.

However, we now think that the taxpayer may be able to pursue a refund claim as to the assessed and paid interest pursuant to the general refund provisions under sections 6511 and 7422.2/ This conclusion follows since section 6621(c) interest

2/ Even if it is determined that the taxpayer may not be able to pursue a refund claim as to the assessed and paid interest under section 6621(c), the Service would still take the position that

is an affected item and not a partnership item per se; therefore, arguably the TEFRA refund provisions do not provide the exclusive refund forum for challenging a section 6621(c) assessment. Compare I.R.C. §§ 6230(d)(6), 6511(g), 6512(b)(3), 7422(h).

We will continue to study the need for recommending legislative changes to deal with the problems presented by the present confusion surrounding section 6621(c)(4). Additionally, the matter could possibly be cleared up by changes in the regulations (e.g., providing in the TEFRA regulations that the determination of whether an underpayment is attributable to a tax motivated transaction is a partnership item which therefore could be the subject of a notice of final partnership administrative adjustment). Therefore, we are giving both of these avenues due consideration and will continue to do so in connection with this matter.

If you have any further questions about this matter, please contact C. Ted Sanderson on (FTS) 566-3233.

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section 6621(c) would not be included in an affected items SND under the above described scenario. This is because, as stated above, the court lacks jurisdiction to determine the applicability of section 6621(c).